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## The critical aspects of Lithuanian competition policy in relation to cartels

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### Abstract

Competition in the market is an essential prerequisite for ensuring the national economic growth; therefore, almost all market economies consider national competitiveness as a value and protect it. The national competition policy, directed towards the detection and punishment of cartels, is an important tool for ensuring fair and free competition and an important factor for maintaining the country's economic development. The success of an efficient competition supervision is determined by not only a formal coordination of the legal basis, but also by the peculiarities of practical application of competition law, economic and cultural aspects of society, the political will and many other factors. Despite the fact that formally, the regulation of competition restricting agreements concluded between undertakings in Lithuania is essentially the same as in the European Union, however, in Lithuania the level of competition culture and competition policy dissemination and public awareness is quite low, compared to the other European Union states. This paper analyzes the aims, measures and mechanism of implementation of the Lithuanian competition policy in relation to the cartels in the context of the EU and highlights the economic aspects, peculiarities and critical issues of this policy.

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## 1. Introduction

In the market economy, competition is an essential prerequisite for operating in the market. Only thanks to competition it turns out which business idea and its implementation in the market is successful and which is not, because, according to Hayek (2010), competition is important as the discovery procedure for entrepreneurs, while searching for unexploited opportunities. So, competition is a value, because through it the allocative efficiency of resources and products distribution can be achieved. However, not all undertakings act fairly. Often, business participants, in pursuit of their selfish purposes (to get more profit, gain a bigger share of the market, reduce market risk, limit the number of competitors, etc.), by their actions distort the "healthy" competition, thus undermining the welfare of both the consumers and other market participants, and in the end, it has a negative effect on the overall economy. The government can not stay away, so it protects the competition and controls the competition restricting factors through the implementation of competition policy. According to Motta (2007), competition policy includes a set of laws that guarantee that competition within the market is not restricted, and at the same time the economic welfare is not reduced. Sufirin and Jones (2004) defined competition policy as a set of measures, through which the governments promote the formation of competitive market structures, and a fair market participants' behavior. Stanikūnas (2009) approached competition policy as a set of measures, functioning of laws and supervision, facilitating fair competition and ensuring that it is not going to decrease within the market. Despite different, but identifying the same aspects, definitions of competition policy, it is important to emphasize that the policy itself will not ensure fair competition until a viable and effective working mechanism for its implementation is created. Although the roots of the rules, regulating the market participants' behaviour date back to almost 2000 years<sup>†</sup>, but during this period, many countries of the world in the history of their economic development have experienced the outcomes of the monopolies and cartels existence in the market, reducing not only the consumers' welfare, but often leading to the economic, political and social development crisis. The consequences suffered by the states due to the lack of competition in the market, have even encouraged and justified the identification and protection of competition as a value.

The development of modern competition policy began in 1890, after the U.S.A. adopted the Sherman Act, regulating monopolies' behavior and prohibiting cartels. In Europe, the first competition laws were adopted only in the first half of the 20th century - in France after World War I, in Germany, Austria and the United Kingdom - after World War II. According to Cairns (1999), with the development of the European Community a danger emerged that the expanded market would encourage economic entities to avoid the national competition laws applied to them, resulting in the need to regulate the protection of competition across the European Union. So, the original documents of the Community - the Treaty establishing the European Community (The Treaty of Rome)<sup>‡</sup> signed by seven Member States in 1957, was supplemented with the rules, whose one of the goals was to prohibit anti-competitive agreements.

Despite the competition protecting laws, the undertakings often risk to conclude prohibited agreements - cartels, whose primary goal is to obtain maximum profit and eliminate competition between them. It is cartel that is considered the most harmful form of competition restricting actions, regardless of the nature of the agreement, i.e. whether it is an agreement on production volumes, prices, discounts, credit terms, customers, territory or other issues. It should be noted that cartels are harmful not only at the micro (the consumer or individual undertaking), but also at the macro (the whole market or country) economic level. According to the European Commission (2008) estimates, only due to cartels, fixing prices or sharing markets, each year consumers in Europe experience at least from 13 to 36 billion Euros of direct damage. Referring to the data of various estimates (Riley (2010), Vogelaar (2008), Connor and Lande (2005)), cartels artificially raise the price by the average of 20 - 30 %: 17-19 % in the national and 30 - 33 % in international cartels. Cartel hazard is evidenced by prosecution of physical and legal

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<sup>†</sup> According to Berger (1991), the earliest preserved example of modern competitiveness law sources is Lex Julia de Annona, adopted in the Roman Republic in 50 B. C. This legal act defined sanctions for raising grain prices and restricting the supply.

<sup>‡</sup> Now - the Treaty on European Union Functioning (TEUF), Article 101.

persons, the global trends of cartel criminalization and the increasing debate on cartel criminalization in the European Union law.

In a dynamic market, the mechanism of prohibited agreements operation in the market is changing, thus causing changes and amendments in laws, regulations and other legal acts. It is this factor that caused major focus on legal aspects of the cartel agreements regulation in the scientific literature (Novosad and Moiseyev (2012), Almunia (2011), Hüscherlath (2009), Stanikūnas (2009), Motta (2007), Klimašauskienė (2007), Aubert, Kovacic and Rey (2005)). The analysis of the Lithuanian competition policy cartel agreements, both in economic and legal terms directly contributes to raising the level of competition culture, competition protection and creation of the market economy conditions for the national economic development. Meanwhile, there is a lack of work focusing on the analysis of economic aspects of competition policy in relation to cartels.

The objective of this article – to identify the critical aspects of Lithuanian competition policy in relation to cartels, which are important in the formulation and implementation of strategic measures, pointed to reduce the harm caused by cartels to Lithuania's economy.

Research methods - a systematic and comparative analysis of scientific literature, laws and other legal acts and logical analysis.

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## 2. The objectives, reasons and legal regulation of cartel agreements in the EU and Lithuania

National competitiveness is not possible without an efficient implementation of competition law. Therefore, an efficient enforcement of competition law in relation to cartels should be the primary objective included in any national competition policy. In order to analyze and assess Lithuanian competition policy in relation to cartels, it is appropriate to analyze the objectives and causes of cartel regulation and conduct the comparative analysis of laws, regulations and their enforcement procedures in the EU and Lithuania, as well as a statistical review of cartels.

The development of competitive Europe is a priority in Europe<sup>§</sup>, contributed by all EU Member States, including Lithuania. Research studies have proved the existing direct link between the country's level of productivity and competitive nature of the market; so the protection of the fair and free competition principle is essential for ensuring both the growth of productivity levels and being able to resist competitive pressure not only within national but also within international markets. In 1991, McKinsey Global Institute was trying to answer the question of why some countries are rich, whereas others are not. After having reviewed the development of 13 countries (the United States, United Kingdom, France, Germany, Japan, India, Brazil, Korea, Russia, Poland, Sweden and Australia) within 12-year period, it has been established that the national economic progress mostly depends on the increasing productivity, which is closely linked with unrestricted competition in the market. Lewis (2005) argued that if the government's policy tends to restrict competition (even if it is done unintentionally), the efficiently operating undertakings can not substitute inefficient undertakings, therefore, economic growth is slowing down, and the states live in poverty. Therefore, efficient enforcement of competition law is important in pursuing both the EU and national economic policy goals.

The measures that must be taken by the government in order to ensure a fair and free competition, vary: including agreements between undertakings, aimed at restricting competition, or which restrict or can restrict competition, prohibition; prohibition to abuse a dominant position, monitoring market concentration and the corresponding prohibition of concentration, prohibition of unfair competition, monitoring compliance with the statutory fair competition protection rules and responsibility for their infringement. So, one of the measures to ensure the freedom of fair competition, both at the national, European and global level, involve prohibition to conclude agreements between undertakings (competitors) whose goal is to restrict competition, usually called cartels.

Active actions taken by the governing authorities in relation to cartels were encouraged by the fact that such prohibited agreements have a negative effect not only on consumers but also on the overall economy, i.e. its

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<sup>§</sup> Europos Sąjungos sutarties ir Sutarties dėl Europos Sąjungos veikimo suvestinės redakcijos 2010/C83/01. Retrieved from: <http://eur-lex.europa.eu/JOHtml.do?uri=OJ:C:2010:083:SOM:LT:HTML>

development and competitiveness, and are also harmful over both short and long-term periods. The European Commission (2003) maintains that cartels, changing the levels of production volumes and (or) the price, generated by the market economy, reduce social welfare, eliminate efficient distribution and transfer the values, generated by the market, from the customer to cartel participants. Cartels, avoiding competition, can create artificial, uneconomic and unstable industrial structures, lead to lower productivity indicators, impede technological progress and develop a long-term increase in prices. In addition, the weakening of competition leads to the loss of competitiveness and negatively affects the labour market. Due to all the above mentioned reasons the disclosure, prosecution and punishment of cartels is the major goal of the European Commission's competition policy. Thus, the efficient enforcement of competition law in relation to cartels should be the primary objective of each national competition policy. Otherwise, not only goals for the single market and consumer welfare, set forth in the EU treaties, will fail to be achieved, but also the national markets will face similar consequences, intended to avoid in the EU.

When Lithuania joined the EU, the country started to directly apply the EU laws, including competition law. Thus, in Lithuania the legal framework in relation to cartels is essentially the same as in the European Union. It should be noted that Article 5 of the Law on Competition of the Republic of Lithuania (LR CL) prohibits all agreements intended to restrict competition, or which restrict or may restrict competition. In relation to a competition restricting agreement, which may affect trade between the Member States, alongside with LR CL Article 5, the Treaty on the Functioning of the European Union (TFEU), Article 101 applies.

### 3. Cartels detection mechanism: institutions, processes and tools

In the European Union an efficient anti-cartel institutional framework has been established, assigned with adequate powers to detect infringements and prosecute the undertakings who conducted the infringement. The Competition Council of the Republic of Lithuania is one of the members of the system, similar to the European Commission with respect to the available legal instruments designed for identifying and detecting cartels, operating in the territory of Lithuania. The Competition Council of the Republic of Lithuania, having initiated an investigation on the prohibited agreement, shall have to conduct analysis on the infringement contents and evaluation of the evidence, consisting of the following stages: 1) defining the relevant market (in which the main goal is to determine whether the undertakings are competitors), 2) identifying at least two independent undertakings - the agreement participants, 3) setting the undertakings action coordination form (an agreement, association decision, coordinated actions), 4) setting the interaction object or the competition restricting effect. Arguing the composition of infringement defined in the Treaty on the Functioning of the European Union, Article 101, alongside with the elements mentioned, additionally the effect on trade between the Member States should be identified.

1) According to the Law on Competition of the Republic of Lithuania, Article 3, Chapter 1, a relevant market is approached as „the market of certain goods in a relevant geographic territory“. The main purpose of defining the relevant market is to identify the competitors of the examined undertakings, who may restrict their freedom to act independently of other market participants. First, the product market is defined by identifying the products that are or may be replaced by another one. Further, the geographical market is defined, by identifying the area where such a substitution takes place or may take place. After the relevant market is defined, the market participants are identified. It should be noted that defining the relevant market is not an end in itself. The accuracy and detail of the market definition depends on the nature of infringement. This conclusion has been repeatedly confirmed by Lithuanian<sup>\*\*</sup> and EU<sup>††</sup> courts, when while dealing with the horizontal price fixing, it is sufficient to establish that the undertakings are competitors, as the price-fixing agreement between competitors itself is already considered an offense.

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<sup>\*\*</sup> The Supreme Administrative Court of Lithuania (SACL) decision in case No. A520-1301/2012 (Orthopedics case), 17/05/2012

<sup>††</sup> E.g. The European Court of Human Rights (ECHR) judgment in case No. T/61/99 *Adriatica di Navigazione* (2003), 11/12/2003, ECR II-5349, 28-29 p.

2) Identification of two or more undertakings - participants of the agreement. According to the CJEU established jurisprudence, the concept of an undertaking in the EU competition law is functional. This means that some individual's compliance with characteristics, attributed to the undertaking, is judged not by its legal form, but rather by the nature of its operational activities. Therefore, the main criterion for identifying an undertaking in the market is its conducted economic activity. On average, 8 undertakings were involved in international cartels fixed by the European Commission (EC, 2013), whereas on average 10 undertakings were involved in cartels, detected by the Lithuanian Competition Council (2013).

3) Defining the undertakings action coordination form. Article 3, Chapter 15 of the Law on Competition of the Republic of Lithuania defines agreements as "contracts concluded in any form (written or verbal) between two or more undertakings or concerted actions of undertakings, including decisions made by any combination (associations, amalgamation, consortium, etc.) of undertakings or by representatives of such a combination". Lithuanian and EU competition law distinguishes three forms of prohibited agreements: agreements, associations' decisions, coordinated actions. The aim of such a division is to prohibit any form of the undertakings action coordination, which, even before reaching the stage of a formal agreement, deliberately substitutes competition risks by practical cooperation. As Lithuanian practice shows, cartel agreements are often concluded via associations, and even they themselves are active members of the cartel. During the period of 2000 – 2012, fines were imposed on 6 associations: Lithuanian Chamber of Auditors (2007), Lithuanian Association of Communication Agencies KOMMA (2009), Packaging and Electronic Waste Management Association (2009), Lithuanian Kennel Society (2010), Orthopedic and Rehabilitation Services Providers' Association (2011) and Lithuanian Shipbrokers and Agents Association (2011).

4) Defining the purpose of interaction or the competition restricting effect. Prohibited agreements between undertakings are divided into agreements which restrict competition by the object and by the effect. Restricting competition by the object – these include such restrictions, which, referring to the objectives of the EU competition law, have such a great potential to negatively affect competition, that the provisions of Article 101, Paragraph 1 of the Treaty on the Functioning of the European Union can be applied without the evidence of the effect on the market (EC, 2011). According to provisions of Article 5 of the Law on Competition of the Republic of Lithuania (1999), agreements between undertakings on fixing the price and sharing markets, intended to restrict competition, restricting or may restrict competition are prohibited. According to the Law on Competition of the Republic of Lithuania, Article 5, Paragraph 2, the agreements concluded between competitors on fixing prices, sharing the market, restricting production or sale volumes, discriminating other individual undertakings, in all cases, shall be considered as restricting competition. Thus, having defined that the purpose of an agreement is to restrict competition, it is not necessary to prove the real effect of such an agreement or action on competition. This position is maintained by the European Court of Justice and Lithuanian courts. In the period of 2000 - 2012, the European Commission has detected the existing 79 international cartels, involving 481 undertakings. The numbers of cartels and their participants detected in Lithuania are presented in Figure 1.

During the analyzed period, 31 cases of cartels were detected in Lithuania, including 5 infringements fixed not only under provisions of the Law on Competition of the Republic of Lithuania, Article 5, but also under provisions of the Treaty on the Functioning of the European Union, Article 101, Paragraph 1. When applying the provisions of TFEU Article 101, Paragraph 1 in relation to prohibited agreements, it is necessary to assess whether the agreement shall affect trade between the Member States. In practice, the arrangements for import, export, as well as agreements creating barriers to the establishment of an undertaking, especially for the undertakings from other Member States, agreements covering the entire territory of a country as well as covering territories of two Member States, by their nature are likely to affect trade between the Member States.

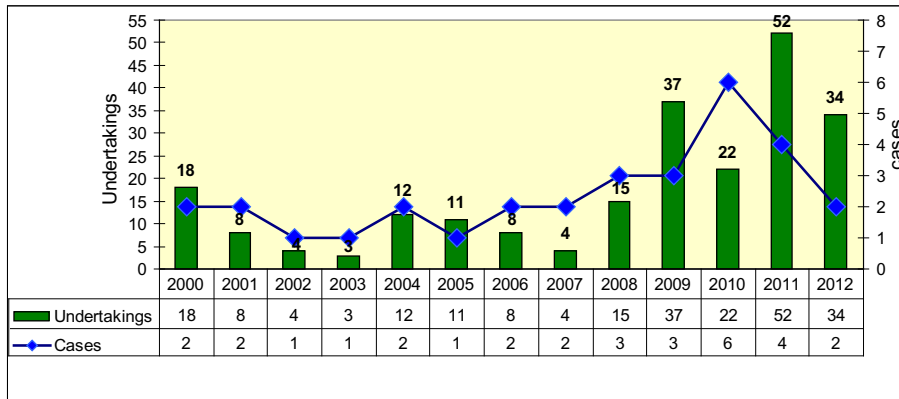


Fig. 1. Prohibited agreements detected in Lithuania and the number of collusive undertakings

Evaluating the Lithuanian competition policy, it should be noted that it is becoming more tough - more cartels are detected and the amount of fines imposed is increasing; for example, in 2011 fines imposed on 4 cartels amounted to 4.36 million Euros, which made 16.5% of the amount of fines imposed in the period of 2000 – 2012; in 2012 fines imposed on two cartels (18.12 million Euros) made 68.6 % of the total sum of fines. Detection and punishment of cartels is just one side of competition policy; the other side of competition policy includes cartel prevention measures, the publicity of competition law and the increasing cultural level of competition.

In general, it can be concluded that both the legal regulation of cartels and legal regulation practice in Lithuania is basically consistent with the European Union's competition law and practical application of law. Although the Law on Competition is in effect for just more than a decade and in Lithuania the competition supervision practice is still developing, but it should be noted that it rapidly improves and develops, following the successful competition surveillance models of the European Union and other countries. The tightening of competition policy and cartel prosecution tendencies are inherent in Lithuania as well.

#### 4. Conclusions

Legal regulation of cartels in Lithuania is basically consistent with the European Union's competition law and practical application of law. The main legislation, applicable for the detection of cartels, includes the Treaty on the Functioning of the European Union, Article 101 (before 2008 - EC Treaty, Art. 81) and Law on Competition of the Republic of Lithuania, Article 5.

In competition law theory and practice, horizontal agreements (price fixing, restriction of production and sales volumes and sharing the markets and customers, including all the above types of agreements in public procurement) are considered as per se restricting competition, because objectively their establishment has no other goals than the restriction of competition. In practice, it is sufficient for the competition supervising authorities just to establish the fact of the cartel existence, and the effect on the market is not assessed.

The European Union has developed an efficient institutional framework of anti-cartel enforcement, with adequate powers to detect infringements and prosecute undertakings – the perpetrators. The Lithuanian Competition Council is one of the members of the system, possessing similar available legal tools to identify and detect cartels operating in the territory of Lithuania, as the EU Commission.

Although the Lithuanian competition policy measures comply with the EU competition policy, its efficient implementation in Lithuania is impeded by the lack of the competition law expertise and culture - competition is not considered as a value not only by Lithuanian undertakings, but by public institutions as well, which may precondition or fail to prevent cartel activities. Therefore, for implementation of competition policies it is important not only to apply criminal leverage in relation to cartels, but also to prevent cartels - by preventing prohibited

agreements and thereby promoting "healthy" competition. In addition, the detection of cartels and their punishment do not guarantee that the economic damage caused by cartels will be compensated and have a deterrent effect in the future.

Aiming to reduce the harm caused by cartels to Lithuania's economy, it is recommended to include the prevention, detection and punishment of cartels into the Lithuanian competition policy priorities. In order to effectively and successfully implement this priority, it is purposeful to follow these directions: 1) improving indicators of cartels detection; 2) practical application of dissuasive sanctions for cartels; 3) increasing the effectiveness of the exemption from fines program in relation to cartel informants; 4) raising the level of competition culture, 5) strengthening the private competition policy enforcement in relation to cartels; 6) ensuring the independence and institutional strengthening of the Competition Council of the Republic of Lithuania.

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